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ATTACHMENT 4: CURRENT FINANCIAL STATUS OF FACILITIES-BASED NEW JERSEY CLECS IDENTIFIED BY VERIZON

| <u>NJ Facilities-Based CLEC</u> | <u>Change in Mkt. Cap.¹</u> | <u>Current Financial Situation</u> |
|--|--|---|
| Broadview Networks | | Never generated positive cash flow; ² laid off more than 90 employees in September 2001; ³ withdrew IPO offer in Fall 2000. ⁴ |
| eLEC (Essex Communications) | - 71.64% | Hearing on Nasdaq's potential delisting of stock to be held January 31, 2002; ⁵ lost \$4.1 million in first three quarters 2001. ⁶ |
| Network Plus | - 95.33% | Reported 2 nd Quarter \$4.9 million EBITDA loss. ⁷ |
| AT&T | - 13.84% | Announced in January 2002 plans to record \$1 billion 4 th Quarter 2001 restructuring charge and expects to eliminate 5,000 employees in 2002, after cutting 8,000 in 2001. ⁸ |
| WorldCom | - 36.94% | Reported 3 rd Quarter 2001 decline in net profit of \$460 million (41%); ⁹ stock value declined 73% in 2000, remained stagnant in 2001; ¹⁰ reported in July 2001 decreased net income of 85%, earnings decrease of 26%, revenue decrease of 4.6%, and lowered outlook for full year, while MCI Group reported net loss of \$29 million and revenue decrease of 15%; ¹¹ laid off 6,300 employees (6-7% of workforce) in February 2001, ¹² 361 in March 2001, ¹³ and 832 in April 2001. ¹⁴ |
| Adelphia Business Solutions | - 96.15% | Announced in January 2002 no dividend payments forthcoming on preferred stock following Salomon Smith Barney report that it faces "near-term restructuring or bankruptcies;" ¹⁵ rumors of impending bankruptcy have caused stock to plunge and cut off new capital; ¹⁶ rumors of likely acquisition by larger entity. ¹⁷ |
| Allegiance Telecom | - 77.53% | Reported 3 rd Quarter 2001 loss of \$106.5 million; ¹⁸ reported 2 nd Quarter 2001 loss of \$103 million; ¹⁹ Moody's announced in October 2001 review to determine downgrading credit rating; ²⁰ lost \$275.5 million for year 2000. ²¹ |
| Cablevision Systems Corp. | - 39.63% | Announced in December 2001 plans to take a \$55 million 4 th Quarter 2001 restructuring charge and eliminate 600 jobs (4% of work force); ²² rumors of likely acquisition by larger entity, including possibly AOL Time Warner; ²³ reported 3 rd Quarter 2001 loss of \$77.1 million ²⁴ and 17% drop in cash flow. ²⁵ |
| Cavalier Telephone (Conectiv Communications) | | Cavalier purchased Conectiv Communications in November 2001, at an expected loss of \$100 million to \$125 million to Conectiv; ²⁶ called off planned merger with two other CLECs in August 2000 due to decline in Nasdaq market. ²⁷ |
| CoreComm (ATX Communications) | - 96.65% | Reported 3 rd Quarter 2001 loss of \$51 million; ²⁸ lost \$313.8 million in 2000; ²⁹ Nasdaq has sought to delist stock since July 2001 and may do so in January 2002; ³⁰ closed Ohio office and discontinued service there, eliminating 180 positions, in August 2001; ³¹ eliminated 110 jobs in July 2001; ³² cut 210 jobs in May 2001. ³³ |
| Focal Communications | - 96.47% | Reported 3 rd Quarter 2001 loss of \$63.7 million and substantially lowered revenue expectations for 4 th Quarter 2001 and year 2002; ³⁴ barely staved off bankruptcy with \$450 million |

| | | |
|-------------------|----------|---|
| | | recapitalization in August 2001, ³⁵ lost \$105.9 million for year 2000. ³⁶ |
| PaeTec | | Canceled planned initial public offering in early 2001. ³⁷ |
| XO Communications | - 99.52% | Delisted by Nasdaq and erased value of public stock as part of \$800 million restructuring plan to avoid bankruptcy, ³⁸ reported 3 rd Quarter 2001 loss of \$50.8 million and Standard & Poor's downgraded credit rating in November 2001, ³⁹ announced in October 2001 elimination of 600 jobs (8% of workforce) and reported 2 nd Quarter EBITDA loss of \$70.7 million, ⁴⁰ posted 1 st Quarter 2001 loss of \$443.5 million (\$1.31 per share), cutting \$2 billion from planned capital expenditures over the next five years, halting European expansion, delaying some domestic expansions, and curtailing some costly services that had limited potential. ⁴¹ |

¹ The figures in this column represent the percentage below the 52-week high for the respective publicly-traded stocks, as calculated by Morningstar.com at the close of trading on January 7, 2002.

² Peter J. Howe, 'New Voice Over DSL' Launch Set in Boston, THE BOSTON GLOBE, October 29, 2001, available in 2001 WL 3959112.

³ Tim Knauss, *Caverns to Store Natural Gas*, HERALD AMERICAN, September 23, 2001, available in 2001 WL 5565702.

⁴ Lisa Bransten, *Deals & Deal Makers: Venture Capital Flows On, Despite Jitters*, THE WALL STREET JOURNAL, November 1, 2000, available in 2001 WL-WSJ 26615197.

⁵ Nasdaq to Delist eLEC, COMMUNICATIONS TODAY, January 2, 2002, available in 2002 WL 6535760.

⁶ Elec Communications Subject to Potential Nasdaq Delisting, DOW JONES (December 26, 2001) <<http://news.morningstar.com/news/PR/M12/D26/1009407660920.html>>.

⁷ Network Plus Moves Into EBITDA Positive Territory, COMMUNICATIONS TODAY, October 23, 2001, available in 2001 WL 29446331.

⁸ AT&T Expects to Take \$1 Billion 4th-Quarter Restructuring Charge, DOW JONES (January 4, 2002) <<http://news.morningstar.com/news/PR/M01/D04/1010180462645.html>>.

⁹ Victoria Furness, *WorldCom helps keep managed hosting services provider afloat*, COMPUTER BUSINESS REVIEW, December 12, 2001, available in 2001 WL 27998787.

¹⁰ Robert Shoenberger, *Most of state's publicly-traded firms buck national trend*, CLARION-LEDGER, December 30, 2001, available in 2001 WL 32321604.

¹¹ See *WorldCom Group's Net Tumbles 85%; Company Reaffirms Lowered Outlook* (July 26, 2001) <<http://news.morningstar.com/news/DJ/M07/D26/96155845910.html>>.

¹² See Reuters, *WorldCom Gives Pink Slips to About 6,000 Workers* (Feb. 28, 2001) <<http://quote.fool.com/news/symbolnews.asp?symbols=WCOM&currticker=WCOM&format=decimal&lpp=10&dtfrom=1%2F19%2F2001+3%3A13%3A28+PM&dtto=4%2F19%2F2001+3%3A13%3A28+PM&sourcetype=1&exc h=NYSE%2CNASDAQ%2CAMEX%2CMF%2CU%2CUS%2CUSMF&cdnsortby=Date&sid=594246&pos=97&action=gs>>.

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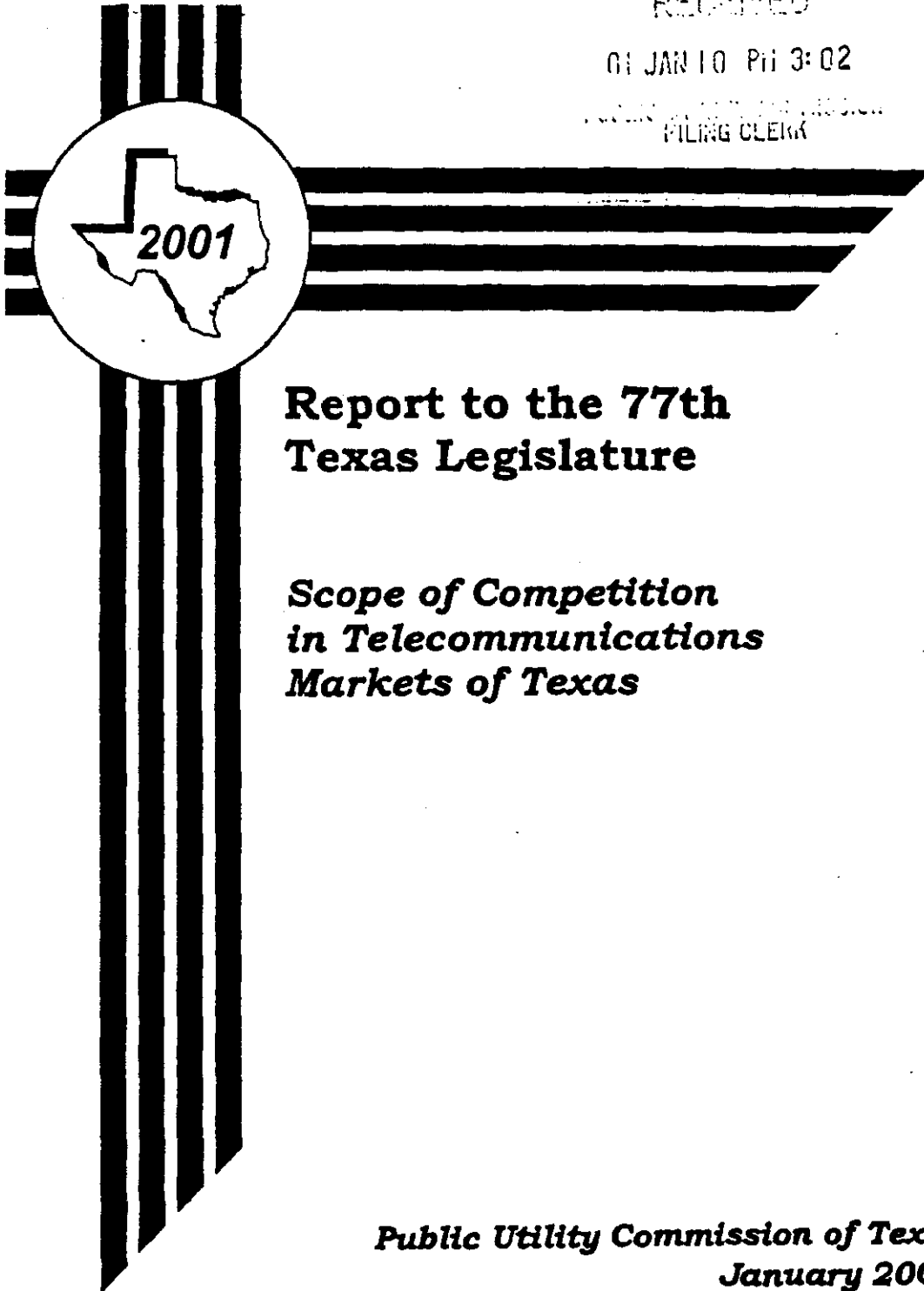
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**Report to the 77th
Texas Legislature**

***Scope of Competition
in Telecommunications
Markets of Texas***

***Public Utility Commission of Texas
January 2001***

33

Pat Wood, III
Chairman

Judy Walsh
Commissioner

Brett A. Perlman
Commissioner

W. Lane Lanford
Executive Director



Public Utility Commission of Texas

January 11, 2001

Honorable Members of the Seventy-Seventh Texas Legislature:

We are pleased to submit our 2001 Report on the Scope of Competition in Telecommunications Markets, as required by Section 52.006 of the Public Utility Regulatory Act (PURA).

Since we issued our previous report on telecommunications competition in January 1999, the Commission has continued to make significant progress in managing the transition to competitive local telecommunications markets. Numerous new providers have entered the market, and the market share held by competitive providers has increased significantly. Recent developments, however, have shown that some of the new providers are having difficulties staying in the residential local exchange market.

In the four largest metro areas of Texas, facilities-based competitors have developed increased capacity for long-run competition with incumbent providers. As a result, the market for business customers in these metro areas has strong potential for genuine competition, although market penetration levels are too low to conclude that full competition has arrived. Whether residential and rural customers will have competitive choices is more uncertain.

Chapter 6 presents an economic diagnosis for why residential and rural customers have largely been left behind in the move to competition. The regulatory tradition of maintaining low (often below cost) rates for residential local telephone service is the key reason. As outlined in the Executive Summary and discussed in its first legislative recommendation, the Commission presents the Texas Legislature with several alternative strategies to create greater opportunity for residential and rural customers to benefit from local exchange competition.

We look forward to continuing to work with you on this and other policy objectives. If you need additional information about any issues addressed in the report, please call on us.

Sincerely,

A handwritten signature in black ink, appearing to read "Pat Wood, III".

Pat Wood, III
Chairman

A handwritten signature in black ink, appearing to read "Judy W. Walsh".

Judy W. Walsh
Commissioner

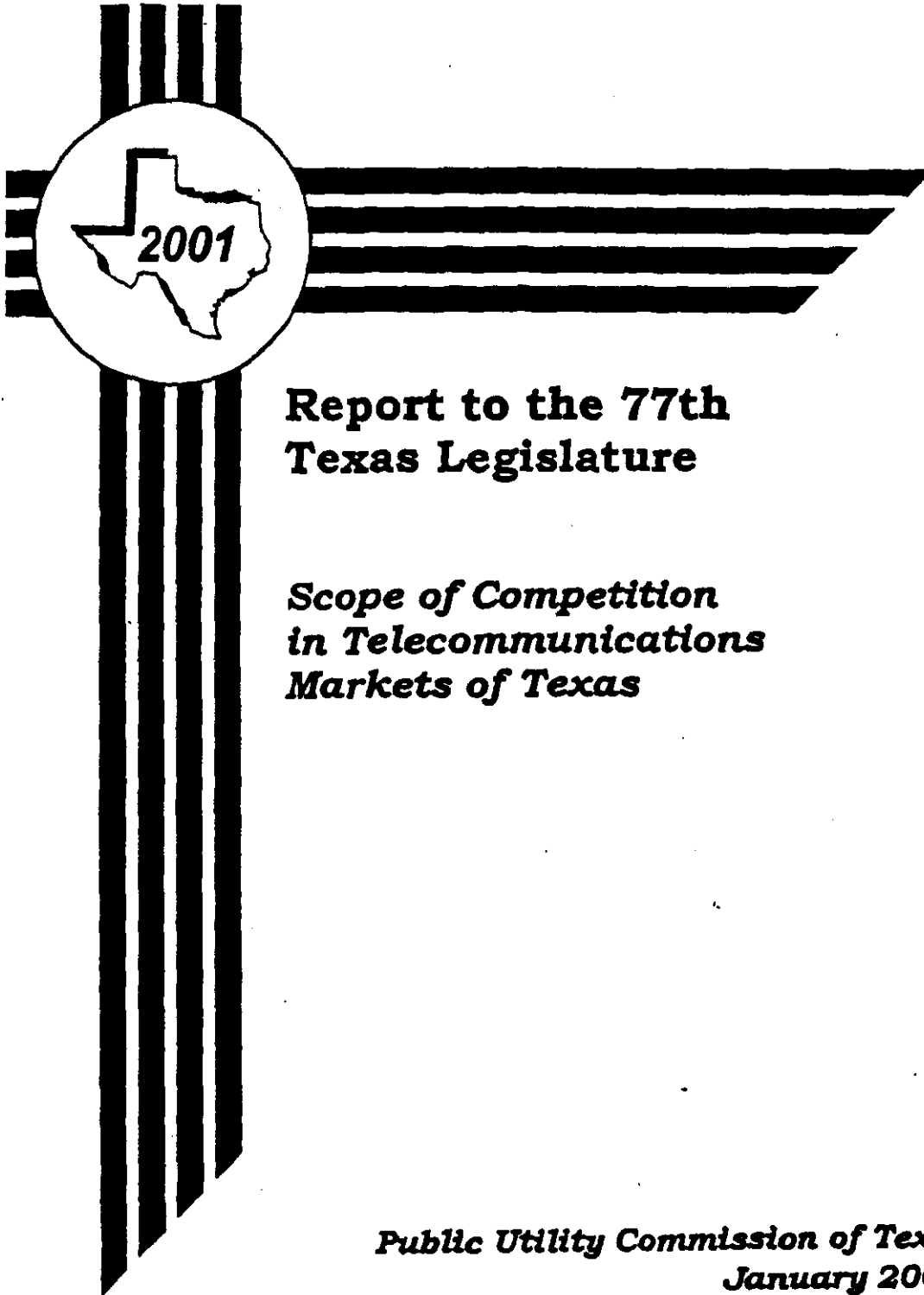
A handwritten signature in black ink, appearing to read "Brett A. Perlman".

Brett A. Perlman
Commissioner



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**Report to the 77th
Texas Legislature**

***Scope of Competition
in Telecommunications
Markets of Texas***

***Public Utility Commission of Texas
January 2001***

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EXECUTIVE SUMMARY

Competitive local exchange carriers now have the regulatory framework to challenge Southwestern Bell and Verizon for market share in Texas. The Public Utility Commission of Texas (Commission) has certified several hundred new entrants, and those in operation have gained visible market share. While the potential for genuine competition is strong for some markets in Texas, it is less likely to flourish in others. At this time, residential and rural customers are better served by existing price cap regulation of traditional nonbasic local service until more viable and sustainable competitive choices become available to them. The Commission recommends finding the proper balance between protecting residential customers in the short run and promoting competition in the long run for the local exchange residential market.

Progress in Local Exchange Competition

During the last few years, the Commission successfully implemented federal and state legislation to open the service territories of the incumbent local exchange carriers, and competitors have responded to the opportunity. As part of the proceedings that led to the approval of Southwestern Bell's application to enter the long distance market, the Commission approved the Texas 271 Interconnection Agreement (T2A), which provides for a standardized, efficient, and quick way for competitors to enter Southwestern Bell's service territories. The availability of such an agreement is a necessary first step to facilitate the entrance of new competitors into the marketplace. Sprint has voluntarily agreed to develop a standard agreement, but other incumbent local exchange carriers – those serving primarily rural areas – are not similarly situated due to the federal exemption for rural carriers from most competition-related requirements. Survey data show that, as of the end of 1999, competitive providers rapidly gained market share in local telephony, as measured in telephone lines operated and in revenues earned. Market penetration is highest in the large metro and suburban areas of Austin, Dallas, Houston, and San Antonio, with more than 30 competitive providers in each metro area by late 2000. Many smaller and medium-sized metro areas, such as Abilene, Beaumont, and Longview, had six to ten competitive providers offering services. Market penetration by competitors in rural areas is very limited, although increasing relative to 1997.

Competitors gained market share among business customers more than among residential customers. Facilities-based competition in the four largest metro areas has provided increased capacity for competitors to compete with incumbent providers in the long run. As a result, the market for business customers in the large metro areas of Texas has strong potential for genuine competition, although the levels of market penetration as of 1999 are too low to declare that full competition has arrived. Whether residential and rural customers will have sustainable competitive choices in the near future is less certain.

Events in the year 2000 have changed conditions for local exchange competition in Texas and across the nation. Competitive local exchange company (CLEC or competitor) stocks have seen a slump in share prices. AT&T, Sprint, and Worldcom announced major company reorganizations with decreased focus on serving residential mass markets. These events suggest that competitors may be heading for a period of consolidation – between companies and within markets. A number of key competitors that were expected to challenge Southwestern Bell and Verizon now seem to be limiting their entry into general residential voice markets.

Because Southwestern Bell can now compete for long distance customers in Texas, the company has made a strong push in 2000 to bundle its offerings to provide residential customers with various options for “one-stop shopping.” Using the pricing and packaging flexibility that SB 560 provided, Southwestern Bell raised prices on the majority of its vertical (nonbasic) telephone services for both residential and business customers while lowering prices for nearly a third of those services listed in this report. Southwestern Bell also gained a sizeable portion of the long distance market just months after offering long distance service for the first time. Southwestern Bell’s largest and strongest competitors have not been offering substantial competition in vertical services or in bundling local residential services with long distance or other services and have lost market share in long distance service.

While opportunities are in place for CLECs to compete in most areas of Texas, the Commission recognizes that differences in customer characteristics and population density among various regions of Texas affect where CLECs decide they can profitably compete and the type of customers they serve. The willingness of the incumbent local exchange company to work with CLECs is also a factor. At the same time, cross-subsidies that have traditionally kept residential rates artificially low now contribute to the lack of competition for residential customers. The same cross-subsidies have provided cream-skimming opportunities in large metro and business markets.

While the possibilities of competition for local service using traditional wireline are mixed at best, technology is reshaping the competitive landscape of telecommunications. New technologies such as cable, wireless, satellite, and voice over Internet Protocol likely will create new avenues and providers for customers to receive traditional local and long distance voice services, profoundly changing the market structure from the customers’ point of view at some point in the future.

Next Step for Local Competition in Texas

The *2001 Scope of Competition Report* summarizes the path taken to open century-old monopolies as well as the use of new tools for facilitating competition that the Texas Legislature provided last session. As detailed above, the response has been good in some markets and disappointing in others. The conclusion today is that competition looks viable in the business and urban markets, but may not be as viable for certain rural and residential customers. The *Report* offers an economic diagnosis for why this pattern has developed, with the primary causes rooted in underlying market conditions and in the historical regulatory pricing system for local telephone service.

Texas has had a long-standing public policy to provide universal service and to maintain low rates for basic residential local service. However, continuing this policy means that some segments of the market may not receive rates that reflect the true cost of the service. In the short term, these segments - most notably residential and rural customers - may need protection from price increases if the market does not effectively moderate them. Indeed, further action may be necessary to ensure that competition comes to these markets at all. The Commission recognizes that short-term remedies are not long-term solutions in regulating a telecommunications industry that is rapidly evolving away from selling simple voice service.

There are a number of ways Texas can go from here. Approaches can be passive or active. The Commission suggests that the Legislature consider the following options for addressing the lack of competition in Texas local residential and rural markets:

Option A: Passive Erosion (no change to current pricing structures).

This is the de facto policy now in effect. If the market is left to behave under current policies, residential customers will continue to have low rates for basic service, but incumbent carriers likely will raise rates further on nonbasic services with little competition under the pricing flexibility granted in SB 560. The economic term for the process of aligning rates to reflect actual costs is called rebalancing. A benefit of allowing these rates to rise is that higher rates for the total set of residential services (even with basic service rates held artificially low) would provide CLECs incentives to offer competitive bundled service packages and to bring new technologies to more areas of Texas. As a result, CLECs may be able to erode the market share of incumbents over the long term.

However, a likely consequence of this approach is that CLECs will serve profitable high-end residential customers and the remaining customers, especially low-end residential and rural customers, may experience price increases for commonly used services for which there are no affordable substitutes at this time. So, while the bundled price of residential telephone services may move closer to its true cost for some customers, the burden of rebalancing prices would continue to be borne by the vertical services user, while basic local services remain subsidized below true cost. From the public's point-of-view, this arrangement may be preferable to having that burden be borne by all residential dial-tone customers.

Option B: Place a temporary, two-year price cap on popular nonbasic residential services that do not currently have competition, and evaluate whether further steps are necessary at the close of the cap to ensure competition in these markets.

This option borrows from both laissez-faire and regulatory economics. Placing caps on residential call forwarding, caller ID, and call return, - the prices of which have increased substantially since SB 560 became effective - would moderate the burden borne by residential customers during the transition to competition for local exchange markets.

Most residential and rural customers receive basic local services at rates well below their true cost (with the remainder of the cost subsidized by Texas and federal universal service payments and over-priced vertical or nonbasic services). The best hope

many of these customers have for competition is from alternate technologies – such as wireless, satellite, or cable – that are not yet cost-competitive with landline basic local service. Landline local exchange competitors may never be competitive with incumbent-provided basic local service at current, subsidized rates. Therefore, the primary benefit of price caps on nonbasic services would be to temporarily protect residential customers from further price increases for services that have already seen large price increases. Such a strategy would allow the opportunity to see if the bundled local service package is priced high enough to allow more competitors to serve more residential and rural customers.

A disadvantage of this approach is that competitive providers need sufficient profit to fight for and win market share from incumbent carriers. Caps on vertical services will also affect competitors' profits slowing innovation in telephony services. At the present time, the Commission has observed that incumbent carriers are often charging prices for nonbasic services that are 5 to 10 times higher than their costs and, in some cases, 100 times higher than their costs. Capping prices at these levels would not limit opportunities for competitors to enter the market profitably.

Option C: Authorize and direct the Commission to hold a proceeding to rebalance costs into a structure that gives competitive providers the incentive to compete in residential and rural markets.

Most residential customers get a majority of their basic local services below cost. Rebalancing of rates would establish residential and rural rates that more closely, reflect the true costs of service. CLECs would have greater incentives to enter new markets in Texas with a wider range of sophisticated services for customers outside the large metro areas. Higher, rebalanced local rates would give local service providers much more economic headroom to deploy advanced telecommunications technologies and services for rural and residential customers.

This approach, however, has several drawbacks. After years of subsidized low rates, many customers would face increases in basic service rates as a result of rate rebalancing. Determining the proper, cost-based price for basic service in a given area would be difficult. Raising the rates for basic local services to meet costs might not permit competition anyway, as lower income and sparsely populated areas of Texas may never be profitable enough to attract competitors in traditional local service for reasons other than retail pricing.

Option D: Combine Options B and C

Combine Options B and C for a comprehensive solution that includes the short-term protection of price caps and the long-term incentives of rebalancing prices to more fully reflect costs. The advantage of this approach is that any negatives associated with the moratorium on certain residential service prices under Option B can be evaluated and adjusted in the course of rate rebalancing. Furthermore, such a proceeding and its implementation are likely to take most of the two years of the Option B moratorium. The cap on prices may mollify negative public reactions that otherwise could result from higher prices, while allowing residential and rural customers to reap the benefits of a wider range of telephone services in the future.

While one of these approaches may be desirable, the Commission believes that long-term re-regulation of residential and rural markets should not be necessary. While monopoly power is still a factor in residential and rural markets at this time, new technologies appear to have the potential to stimulate vigorous competition in a number of parts of Texas in the years to come. Until then, the Legislature's price cap on traditional phone services serves as an appropriate customer protection.

CHAPTER 1: LEGISLATIVE PARAMETERS FOR LOCAL COMPETITION

The beginning of local exchange competition in Texas is evident. Competitive telecommunications providers now have fair access to networks to provide local exchange service in Texas. Over the past two years, the Commission and interested parties have hammered out the details of a procedural and structural framework for local competition that gives competitors ready access to the Texas markets. The transformation is sufficient to firmly position Texas for the development of long-term, sustainable competition and for increased customer choices in telecommunications services.

Texas met the challenges of federal laws and regulations regarding local competition, which give state commissions great responsibility for their implementation. For example, state commissions must approve or reject agreements among competitors and incumbent providers to interconnect their networks, and they have primary responsibility for arbitrating and mediating such agreements if asked to do so by the negotiating parties. State regulators are also charged with developing and implementing cost-based prices for many provisions of interconnection agreements. While the basic blueprint for local competition is established on the federal level, the front line for implementation is the state level.

A number of the implementation developments in Texas are quite extraordinary, as reflected in the fact that they have been closely watched and are now routinely mirrored by other states. They are the result of contributions by many people representing many constituencies, including new market entrants, incumbent local telephone companies, the U.S. Department of Justice, the Federal Communications Commission (FCC), and the Texas Commission commissioners and staff. All shared a vision of a competitive future for telecommunications in Texas, although each viewed the details from different perspectives and interests. These entities contributed thousands of hours to deliberations and/or negotiations. The result is that many of Texas' nearly 20 million people have at least some choice in the provision of local telephone service.

How and why did we get here? Formative legislation at both state and federal levels set the stage for this transformation. Chapter 1 highlights the relevant history and directives of that threshold legislation.

Key Legislation

TEXAS HOUSE BILL 2128 (A.K.A. PURA 95)

In 1995, the Texas Legislature adopted House Bill 2128 (HB 2128), which significantly amended the Public Utility Regulatory Act (PURA) with regard to telecommunications. It mandated the opening of local exchange telecommunications markets in Texas, particularly in areas served by Southwestern Bell Telephone Company (SWBT) and GTE Southwest Incorporated. The law provided a framework for competitive local exchange carriers (CLECs)¹ to obtain authority from the Commission to provide local exchange service through any of three avenues, including by building network facilities,² leasing local loops,³ or reselling another company's telecommunications services.⁴ Additionally, HB2128 established the duty of telecommunications providers to "interconnect" their networks with each other.⁵

FEDERAL TELECOMMUNICATIONS ACT OF 1996

On February 8, 1996, Congress enacted the federal Telecommunications Act of 1996 (FTA),⁶ which paralleled HB 2128 in numerous ways, and fundamentally changed telecommunications markets for the entire nation. The FTA was the most dramatic change in telecommunications law since Congress passed the Communications Act of 1934. Three principal goals established by the telephony provisions of the 1996 Act were (1) opening the local exchange and exchange access markets to competitive entry; (2) promoting increased competition in telecommunications markets that were already open to competition, including the long-distance services market; and (3) reforming the system of universal service so that universal service would be preserved and advanced as the local exchange and exchange access markets move from monopoly to competition.

TEXAS SENATE BILL 560 AND SENATE BILL 86

The transition from monopoly to competition could not and did not occur quickly. In 1999, the Texas Legislature revised PURA by enacting two bills dealing with the provision of local exchange telephone service. SB 560 increased flexibility for incumbent local exchange companies (ILECs) in pricing and packaging telecommunications services. The Texas Legislature also passed SB86 to ensure customer choices and protections.

¹ Perspectives on CLEC market share are discussed in Chapter 3. Certificated CLECs are listed in Appendix G.

² PURA95 § 3.2531. The remaining part of this section is now in PURA Ch. 54, Subchapter C.

³ PURA95 § 3.453 (now PURA Ch. 60, Subchapter C). In addition, PURA95 § 3.453 (now PURA § 60.021) directed ILECs to unbundle their networks to the extent ordered by the FCC.

⁴ PURA95 § 3.453 (now PURA Ch. 60, Subchapter C).

⁵ PURA95 § 3.458 (now PURA Ch. 60, Subchapter G).

⁶ Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (1996 Act). The 1996 Act amended the Communications Act of 1934. 47 U.S.C. §§ 151 *et seq.* (FTA).

Key Features of the FTA

THE TRILOGY: LOCAL COMPETITION, UNIVERSAL SERVICE, & ACCESS CHARGES

The FCC views the FTA as a trilogy, *i.e.* a three-pronged plan. The first prong of the trilogy consisted of opening local exchange and exchange access markets to competition.⁷ The FTA requires all local exchange carriers (LECs), not just incumbents, to interconnect so that competing carriers can provide service.⁸ The second prong of the trilogy is universal service reform. Consistent with FTA §254, *Universal service*, the FCC believes the universal service support system must guarantee affordable telephone service to all Americans in an era in which competition will be the driving force in telecommunications (*see* Appendix A). The third prong of the trilogy is access charge reform.⁹ Because a competitive market drives prices toward cost, the then-existing system of access charges was unsustainable because access charges were widely believed to be significantly higher than the cost of providing access (*see* Appendix B).

METHODS OF COMPETITIVE MARKET ENTRY

The FTA §251(a)(1) requires all telecommunications carriers to interconnect with the facilities and equipment of other telecommunications carriers, allowing competitors three ways to serve customers.

- **Resale** – Under this entry method, competitors have the option to purchase telecommunications services from another LEC at wholesale rates and resell those services to their own customers at retail rates.¹⁰ Competitors often use resale as a transitional entry strategy while building a proprietary network over a period of months or years.
- **Access of Unbundled Network Elements** – This entry method enables competitors to lease discrete parts of an ILEC's network – facilities and equipment that are used to provide telephone service – at cost-based rates. These leased parts of the ILEC network are referred to as “unbundled network elements” (UNEs). Competitors can combine leased UNEs with their own facilities and/or resold services.

⁷ Opening local markets was accomplished primarily through FTA § 251, *Interconnection*, and § 252, *Procedures for negotiation, arbitration, and approval of agreements*. Additionally, special provisions for opening local markets contained in FTA § 271, *Bell operating company entry into interLATA services*, pertain only to Bell Operating Companies.

⁸ FTA §251(a)(1).

⁹ Access charges are per-minute charges billed by LECs to long distance companies for access to the local exchange network so that long distance companies can originate and terminate long distance calls.

¹⁰ All LECs are required to make their telecommunications services available for resale pursuant to FTA § 251(b)(1). However, only *incumbent* LECs are required, pursuant to FTA § 251(c)(4), to make their retail telecommunications services available for resale at a wholesale discount.

- Construction of New Facilities – A competitor may enter a local telephone market by building entirely new facilities. Under a full “facilities-based” method of entry, a competitor builds all of the network that it needs to serve customers, including the “last mile” or “local loop” – the connection to a customer’s premise. Because telecommunications networks are capital-intensive, there are relatively few facilities-based carriers compared to the number of resellers and UNE-based carriers.

THE SECTION 271 “CARROT”

Section 271 of the FTA allows a Bell Operating Company (BOC) to enter the long distance market after the BOC *proves* that it has opened its local market to competition.

Bell Operating Companies were created in 1984 with the divestiture of AT&T, and were granted monopoly status to provide local service, subject to regulation by the states.¹¹ At that time, BOCs were prohibited from competing in the interLATA long distance market to prevent them from committing anti-competitive practices against long distance providers.

Clearly, the FTA’s requirement that the former monopoly BOCs open their networks to competitors, resulting in a loss in market share and power, was a tall order. Because entry into the long distance market would allow a BOC to offer its customers “one stop shopping,” the Section 271 provisions created an incentive to BOCs to cooperate with the FTA mandate to open their networks to local competition.

FEDERAL-STATE SHARED RESPONSIBILITY FOR IMPLEMENTATION

Implementation of the FTA has led to parallel proceedings at state and federal levels, covering similar issues, in similar time frames, affected by court challenges. Often, interplay across proceedings occurred.

The FTA’s blueprint for encouraging local exchange competition placed great responsibility on the FCC and state commissions to implement the law.¹² Only six months after adoption of the FTA, the FCC produced two comprehensive documents charting a course for implementation. Some of the FCC’s interpretations were challenged in federal court, and many of the FCC’s interpretations of FTA requirements were affirmed. Where specific FCC findings were not affirmed, federal and state regulators adjusted through regulatory rule and other processes.¹³

¹¹ In 1984, there were seven Regional BOCs, made up of a total of 29 BOCs.

¹² Although the FCC establishes nationwide guidelines, state regulators play a major role in implementing key provisions of the FTA. For example, state Commissions must approve or reject interconnection agreements, and they have primary responsibility for arbitrating and mediating such agreements if asked to do so by the negotiating parties. State regulators are also charged with developing and implementing cost-based prices for interconnection and UNEs.

¹³ In its initial Order implementing the local competition provisions of the FTA in August 1996, the FCC established rules about how interconnection between incumbent and competitive carriers would be accomplished, how the competitors would be allowed to collocate equipment in the incumbent’s structures,